



Acquisition Advisory Panel Public Hearing Statement

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On behalf of the

Information Technology Association of America

Good afternoon. My name is Bruce Leinster, and I am appearing today on behalf of the Information Technology Association of America (commonly called the "ITAA"). For those of you who are unfamiliar with ITAA, it is the leading association of information technology companies. ITAA provides global public policy, business networking, and national leadership to promote the continued rapid growth of the IT industry. The ITAA consists of just under 400 corporate members throughout the United States, and a global network of 47 countries' IT associations. The Association plays a leading role in addressing policy and legal issues that affect the IT industry, including government IT procurement. ITAA members range from the smallest IT start-ups to industry leaders.

My comments today are based on my 36 years of service with IBM. Prior to my retirement in 2004, I served as the Director of Contracts for IBM's Public Sector Industry. In that capacity, I managed IBM's team of professional contract negotiators responsible for the negotiation and contract support of all of IBM's unique solutions offered through its Federal Systems Division as well as IBM's vast commercial products and solutions being offered by the company today. In retirement I continue to represent IBM in a consulting capacity.

I have six points I would like to make regarding T&M contracts, and these are as follows:

Point 1. T&M Contracts Are Appropriate Contract Vehicles In Situations Where the Scope of Work Is Not Defined Upfront With Reasonable Certainty.

T&M contracts serve a valuable role in the acquisition process when the factors set out in FAR 16.601 are present; that is, (1) it is not possible at the time of placing the contract or task order to estimate accurately the extent or duration of the work, or (2) it is not possible to anticipate costs with any reasonable degree of certainty. In these situations, T&M or labor-hour contracts may be the only viable contract vehicles. Firm-fixed-price contracts are inappropriate when these factors are present because firm-fixed-price payment terms present an unreasonable amount of risk for contractors and would unduly restrict competition to those contractors willing to assume very high risk. On the other hand, use of cost-reimbursement contracts in these situations may eliminate many commercial

companies wishing to do business with the Government but that do not have the infrastructure in place to comply with Government-unique cost accounting rules.

The reasons why firm-fixed-price contracts are not in furtherance of the Government's interests when the scope of work cannot be defined upfront with reasonable certainty was expressed succinctly by the General Accountability Office in a 1990 decision, captioned Four Star Maintenance Corp., B-240413, Nov. 2, 1990, 91-1 CPD ¶ 70. The Four Star Maintenance case involved a proposed facility maintenance contract that did not reasonably confine the volume of work that the contractor would be required to perform. GAO provided the following rationale in ruling that the use of fixed-price terms was inappropriate:

“[W]e think that the requirement to perform most of the work under the contract at a fixed monthly price involves risks to the contractor and the government that outweigh any advantage it might offer by deterring some unnecessary work. First, if the contractor builds into its prices contingencies to cover the possibility that the work required will exceed the RFP estimates, and the agency ultimately requires less than the estimated work, *the government will pay more* for the work than if payment were based upon fixed quantities or unit prices. Under this scenario, the contract *would not result in the lowest cost to the government*. Conversely, if the contractor bids based on the cost of performing the estimated work, without including the cost of work in excess of the estimates, and the agency ultimately requires work in excess of the estimates, the contractor would be required to perform all additional work at no cost. We think this is *unfair and unwarranted* where not necessitated by some strong agency need.”

GAO reached a similar conclusion in a 1999 bid protest case, captioned, BMAR & Associates, Inc., B- 281,664, March 18, 1999, 99-1 CPD ¶ 62, which involved a fixed-

price solicitation for civil engineering services.

Accordingly, there are contract scenarios where a T&M or labor-hour contract would best serve the Government's interests.

Point 2. It Is Not Always Possible or Desirable to Define the Work Upfront Sufficiently To Provide for a Firm-Fixed Price Contract.

A good example of this is when a contractor accompanies U.S. military personnel during contingency operations or is performing disaster recovery operations. In these situations the duration or the amount of manpower necessary to perform the required services, more likely than not, cannot be estimated with any reasonable degree of certainty. To a lesser degree the same can be said regarding certain IT or facilities support services where there is no reliable historical track record upon which to predict the extent or duration of work or it is otherwise not possible to estimate user or customer demand for the service.

The Panel has asked whether there should be a distinction between providing services identified with a specific task or outcome versus providing services that amounts to "buying people at desks." To the extent the Panel's question is directed at use of T&M terms for such services, we believe that T&M payment terms would be appropriate under either scenario so long as (1) it is not possible at the time of placing the contract or task order to estimate accurately the extent or duration of the work, or (2) it is not possible to anticipate costs with any reasonable degree of certainty.

Point 3. Most Contractors Would Prefer Fixed-Price Contracts if the Scope of Work Is Reasonably Established.

Most contractors would prefer to perform work on a firm-fixed-price basis than on a T&M basis if the scope of work is such that a contractor can reasonably measure the amount of risk inherent in the work. In our view, firm-fixed-price contracts offer the following benefits over T&M contracts:

- Greater management flexibility in performing the work.
- Less Government oversight than compared to T&M or cost reimbursement payment terms.
- The potential for greater returns on investment.

As I have indicated with Point 2, however, it is not always reasonable to attempt to price certain kinds of work on a firm-fixed-price basis.

Point 4. T&M Contract Terms Are Used in the Commercial Marketplace for the Same Reasons They Are Used in the Federal Government Marketplace.

An informal survey of ITAA membership has confirmed that IT service providers often enter into T&M contracts when the work cannot be defined with any reasonable degree of certainty at the outset, where the contractor may be required to ramp up or ramp down quickly as the volume of work changes, or where the project otherwise is too risky for firm-fixed-price bidding. Such contracts may include large IT repair and maintenance services contracts, system integration efforts where the nature of the customer's existing infrastructure has not been defined with reasonable specificity, custom software programming to be provided on an "as needed" basis, and certain IT support services (such as help desks) where the customer is unable to set confines on the volume of work.

For example, as a *buyer* of services, IBM last year acquired approximately \$1.2 billion in technical services on a T&M basis.

There are times when IT service providers are willing to use either T&M or firm-fixed-price terms, provided that they are able to include a sufficient contingency amount in their pricing to cover any risk with respect to the scope or duration of work. Pursuant to the Sarbanes-Oxley Act of 2002, it is the corporation's responsibility to have a system in place to control risks, including risks associated with Government contracts.

Point 5. There Are Significant Incentives in Place that Help Ensure Successful Performance of T&M Contracts.

Some critics of T&M contracts argue that T&M contracts do not provide sufficient motivation for contractors to perform efficiently. But this argument seems to ignore the reality that contractors are subject to significant built-in incentives to perform T&M (as well as other) contracts in a high-quality, efficient manner. For example:

1. Inefficient performance of a T&M contract will result in a poor past performance rating. A strong past performance record is vital to a contractor's efforts to secure future work because past performance is a mandatory evaluation factor on which contract awards are based.
2. A contractor could be subject to termination if it fails to perform commensurate with the standard of performance specified in the contract. For example, FAR 52.232-7, Payments under Time-and-Materials and Labor-Hour Contracts, requires the contractor to use its *best efforts* to perform the work specified in the contract within the ceiling price. Failure to provide best efforts could subject the contractor to termination for cause, a drastic sanction that can be accompanied by significant liability and suspension or debarment proceedings.

3. Failing to perform efficiently and effectively makes it less likely that an agency will exercise contract options or award follow-on work to the contractor.

Moreover, T&M contracts, like other forms of contracts, can include performance-based incentives to ensure high-quality performance. Such incentives could be included in the way of service-level credits and bonuses based on the quality of service.

Point 6. Controls Exist To Ensure that Pricing on Commercial T&M Contracts is Fair and Reasonable.

I would like to emphasize that there are also several controls that exist to ensure that pricing on T&M contracts is fair and reasonable.

First, with respect to Multiple Award Schedules contracts, contractors are required to disclose their commercial sales practices upfront to the Government prior to entering into the contract. If the contractor offers better pricing to any commercial customer, the Government will know about it upfront prior to contract formation.

Second, pursuant to the Service Acquisition Reform Act, commercial T&M contracts currently must be awarded on a competitive basis. The forces of competition further help to ensure that contractors are offering competitive rates. In the event that adequate price competition is not present despite the conduct of a competition, FAR 12.209 and FAR 15.403-3 authorize the contracting officer to request that offerors provide information other than certified cost or pricing data to ensure the reasonableness of the pricing.

Third, management techniques provide the Government and the contractor with insight into whether contract performance is on target for satisfying the Government's objectives, including its cost objectives.

Fourth, as previously mentioned, the contracting parties can agree to include performance-based provisions in T&M contracts. A series of incentives and disincentives may further help to ensure that the Government achieves its objectives.

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In closing, I would like to add one final observation. There seems to be a tendency by some people to want to add to the plethora of procurement-related rules and safeguards whenever an instance of misuse of the procurement system is reported in the press. For example, recent press reports regarding out of scope task orders and the use of commercial terms on allegedly non-commercial items concern possible violations of rules that already exist. In situations where the issue pertains to the failure to follow the existing rules, ITAA believes that adding new rules fail to address the root cause of the situation and serve only to compound the problem. In our view, many of the recent reports involving the use of improper contract vehicles has more to do with a lack of training and education than it has with any gap or weakness in the existing the set of rules.

I would be pleased to answer any questions you may have.